No. 11116

In the United States Circuit Court of Appeals

For the Ninth Circuit

GEORGE M. McBRIDE, Trustee in Bankruptcy of Western Bond and Mortgage Company, an Oregon Corporation, Bankrupt,

Appellant,

vs.

C. H. FARRINGTON,

Appellee.

APPELLANT'S REPLY BRIEF

Upon Appeal from the District Court of the United States for the District of Oregon.

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ANENT, APPELLEE'S PRELMINARY STATEMENT

The appellee, C. H. Farrington, in his Brief, pp. 5 & 6, is critical of the Appellant's Brief in that it is asserted that appellant presents therein his case on the theory that Farrington had been a party to the fraud charged in the complaint. We do so present our case, for obviously under the pre-trial order segregating the trial of the issues of fraud and of limitations and ordering the trial of the latter issue first, the assumption must be made that the frauds alleged in the complaints are true. On no other theory could

the issue of limitations (in which we include laches) be determined. Obviously the court under the order of segregation (Tr. 58) was compelled to assume that the frauds asserted were provable in order to determine whether the statute of limitations had run against suit for recovery.

In the course of the argument in Appellee's Brief, Appellee's attorney, says (p. 6),

> "Although charges of fraud have been hurled against this defendant since 1931, there has never been any adjudication of misconduct on defendants' part in any proceeding, and none in the case at bar."

Such a statement is unwarranted. There is nothing in the Record here, (and that is what we are trying this upon) to justify the statement (1) "that there never has been any adjudication of misconduct on defendant's part in any proceedings" or to justify the statement (2) "that charges of fraud has been hurled against the defendant since 1931."

Moreover, we are at a loss to appreciate the statement that "fraud is never presumed" appearing on the same page of appellee's Brief. May we venture the suggestion that where an officer owning a substantial majority of the stock of a corporation obtains a transfer of property of the corporation to himself that a presumption of fraud follows.

In his Brief, after the preliminary statement, C. H. Farrington urges:

(1) That the appellant's Assignments of Error are insufficient to present any question for the consideration of this Court,

(2) That the findings of fact are not amenable to attack, since some substantial evidence was adduced to support them.

(3) That the evidence adduced showed also that the trustee was guilty of laches barring the suit, and

(4) That the evidence adduced shows that the Trustee in Bankruptcy, appellant, had failed to pursue with reasonable diligence information which had come to him, which information if pursued would have brought knowledge of the frauds alleged, thus barring the suit.

Let us consider these contentions of the appellee in the order stated.

SUFFICIENCY OF ASSIGNMENTS OF ERRORS

What, we ask, is the purpose of the requirement that errors be assigned? Naturally, so that the Appellate Court may know just what particular error is claimed to have been made by the trial court which justifies the appellant in the belief that the cause should be remanded or the judgment be reversed, and also so that the appellee may be able to know and to meet the specific attacks of the appellant. Thus, it is held insufficient to assign as error merely that the Court entered a wrong decree (*Cohen v. U. S.* and

Squibb v. Mallueckrodt Chemical Works, cited and quoted from by Appellee in his Brief, p. 9), or that generally the trial court made wrong findings (*American Surety Co. v. Fischer W. Co.,* also cited and quoted from in Appellee's Brief, p. 8).

However, there is no such generality in the Assignments of appellant here questioned.

Certainly our Assignment I cannot be objectionable. It reads: "The Court erred in determining that the Oregon Statute was the applicable Statute" (see our Opening Brief, p. 18). Is that not specific enough? The determination involved solely a question of law. Is it possible that Appellee insist that we must point out the mental process of the Court that caused it to reach such a conclusion, which we assert to be wrong? We will stand on the assignment.

The next assignment proceeds on the assumption that the Court has determined the applicable statute to be the Oregon Statute prescribing limitation of two years from the discovery of the fraud. We assign in this Assignment (IIa) that the court erred in holding "that the Trustee had not brought the action within two years from discovery." (Our Brief p. 18). Then follows, shortly after in our Brief (p. 24) this statement "There is direct testimony to the effect that the discovery of the fraud occurred only within a month or two after bringing this action, and there is no testimony whatsoever of an earlier discovery."

The third assignment set forth in our Brief (p. 18) is Specification II(b), and that assignment states

that the Court erred in holding "that the information which came to the Trustee charged him with the duty to pursue it." It seems to us that there can be only one implication as to this assignment and that is that the inference which the court drew, was in law an erroneous inference, namely, that the information coming to the trustee charged him with the duty of pursuit. We maintain that such an Assignment of Error meets all the requirements of a sufficient assignment.

The fourth assignment (Our Brief, p. 19), being number II(c), assumes the finding by the Court that there was duty of pursuit, yet assigns as error the holding that "such information if pursued would have resulted in discovery at a time more than two years prior to the institution of the action here". We insist that such assignment is not amenable to the objection of generalization. Quite the contrary, it definitely points to error of law in the Court's holding that in the light of the evidence there would have resulted earlier discovery had the available information been pursued.

The last assignment, being numbered by us III, (Our Brief p. 19) assigns as error the Court's holding "That the Trustee was guilty of laches." That too, we maintain, is a sufficient specification of an error of law, since it is apparent that our position is that there were no facts on which such a finding could have been correctly made. (See discussion of Laches, Our Opening Brief, pp. 35-36.)

AMENABILITY OF FINDINGS TO ATTACK

We are fully aware of the doctrine that where there is a conflict of evidence, and the court makes findings based on some evidence, even though the evidence on which the finding is made be meager and not preponderant, such findings will not be disturbed on appeal. But the findings of fact must be findings of *fact,* and not a mere inference from admitted or found facts or from uncontroverted evidence.

Moreover, it is immaterial that the inference or conclusion be called a finding. Such appellation is of no consequence.[1] Under such circumstance the Appellate Court is as well qualified to make the inference as is the trial court.[2] The subject thereupon becomes a matter of law, and not of fact.

Let us particularize: In the case at bar the Court under the title of Finding of Facts, states "Plaintiff had actual knowledge or was in possession of information which was sufficient to guide him to actual knowledge," (Finding III.) which information he "failed to pursue with reasonable diligence", "and which pointed to the transactions referred to in the Complaint". (Finding IV)

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(1) 5 C.J.S. Appeal and Error 1454, pp. 25-26.

(2) Western Union Tel. Co. v. Brombert (C.C.A. 9th) 143 F. (2d) 288, 290; Stubbs v. Fulton Natl. Bank (C.C.A. 5th) 146 F. (2d) 558, 560; Murray v. Noblesville Milling Co. (C.C.A. 7th) 131 F. (2d) 470, 474; Kuhn v. Princess Lida, (C.C.A. 3rd) 119 F. (2d) 704, 706; Shultz v. Mfg. & Traders Trust Co. (C.C.A. 2nd) 128 F. (2d) 889, 901.

Now is not this whole statement an inference rather than a finding? In the first place, if the plaintiff had "actual knowledge" of the transactions referred to in the complaint, and if he had possession of information which was sufficient to guide him to knowledge" which if followed through with reasonable diligence would have spelled discovery, then the trial court should not have made his "findings" in these regards in the conjunctive. A Court does not correctly make a "finding either or". But that is just what the trial court here did, for he says: "plaintiff had actual knowledge *or* was in possession of information". Obviously, the Court was merely being argumentative, and of course no finding should, or properly can, have such character.

We assert, with assurance, that there was not a scintilla of evidence that the trustee had actual knowledge at any time prior to a few months before suit was brought. In fact all the evidence on that question is to the contrary (Tr. pp. 95-96). Consequently, the so-called "finding" to this effect was either erroneous, or it was merely setting the stage for an inference to the effect that if the trustee did not have actual knowledge he should have had it. That is, we contend, the exact significance of the Court's Findings III and IV. They are really not findings at all, but merely an inference or conclusion from the admitted facts based on undisputed testimony. Such inference, or a contrary one, the Court here can as well draw as could the trial court.

The last "finding" of the court, to which we assigned error, is the finding (VI) that "Prior to bringing of this action, participants in the transactions . . . and others who had known the materal facts had died, and defendant was deprived of a means of defense through their evidence."

We maintain that such a finding is too general a one to make it anything more than a conclusion. What facts were known to whom? Who had died knowing such fact? Would such facts have been favorable to defendant? Was the defendaut deprived of the means of defense by the fault of the plaintiff or merely by the act of God—death?

But, be that as it may, our more specific objection to this "finding" is that it is not based on any evidence. No testimony was introduced to the effect that those who were in any way connected with, or who participated in, the transactions would have given favorable testimony for the defendant. Mr. Arthur Spencer (whose only asserted connection was that he was attorney for the defendant) it was testified to, handled the legal phase of the Western Guaranty Stock transaction for Farrington (Tr. p. 254), but there was no testimony that he knew the facts concerning the alleged fraud asserted in plaintiff's complaint, or that he would have, if alive, testified favorably to defendant's defense. Mr. O'Flynn, it was testified, was also dead. He it was who represented the Massachusetts Mortgage Company, the intermediate purchaser in the alleged fraudulent Western Guaranty Stock deal (Tr. p. 257). But there was no testi-

mony that the facts which he knew would have been helpful to the defendant. (As a matter of fact, the death of Mr. O'Flynn was thought by us, for a time, to be disastrous to plaintiff in the proof of his case.) Judge Carey, it is asserted, is also dead. He was the Corporation Commissioner of the State of Oregon at the time of the transactions. But there is not the slightest intimation in the testimony (albeit, there is such intimation in Appellee's Brief, p. 21) that Judge Carey knew the slightest thing about the transactions set forth in the complaint, or that he could have testified favorably to defendant.

Referee A. M. Cannon is also dead. But it is not even claimed by either of the parties, much less is there any testimony, that Referee Cannon had the slightest knowledge of the transactions referred to. (In Appellee's Brief pp. 22, it is asserted that the death of A. M. Cannon made it impossible to challenge the truth of the testimony of the Trustee—though nothing is said about challenging the truth of like testimony of the trustee's attorney—to the effect that he directed that no objection be filed or pressed to the Government's claim for taxes until there were some assets available in the estate to pay at least a portion of the claim if allowed). The referee's death could only have prevented his testimony concerning the delay or promptness in the discovery of fraud—not in the establishing a defense concerning the fraudulent transactions of Farrington, which of course, was what the "findings" referred to.

Where, then, was the basis for the "finding" that "defendant was deprived of a means of defense" by the death of "the participants in the transactions referred to in the complaint, and others who had known the material facts"?

We maintain therefore, in this case, where the facts are not disputed as to what information came to the trustee, that the ultimate facts as to whether or not such information in the exercise of reasonable diligence should have been pursued and if pursued would have resulted in timely discovery, is a question which this court may determine as well as the trial court. As was said in the case of *Murray v. Noblesville Milling Co.* (C.C.A. 7th) 131 F. (2d) 470, 474 (ante)

> "To be sure where the findings of fact is supporting by evidence and is not clearly erroneous it must be accepted by us but the rule does not operate to intrench with like finality the inferences or conclusions drawn by the trial court from its fact findings and we are free to draw the ultimate inferences and conclusions which the findings reasonably induce, and where the evidentiary facts are not in conflict or dispute, the conclusions to be drawn therefrom are for the appellate court upon review."

To like effect also is *Kuhn v. Princess Lida* (C.C.A. 3rd) 119 F. (2d) 704, 706 (ante), where it is said:

> "Where the evidentiary facts are not in conflict or dispute, the conclusions to be drawn therefrom are for the appellate court upon review of the trial court's action . . . An incorrect conclusion by a trial court qualifies as a 'clearly erroneous'

finding, for the correction whereof on appeal Rule 52(a) specifically provides."

LACHES—NO EVIDENCE JUSTIFYING THE HOLDING

Appellant in its Brief takes issue with our statement that if the present action is not barred by the Statute of Limitation it is not barred by laches. We still insist that such is true in this particular case, and we again revert to the case of *Sedlak v. Sedlak*, 14 Or. 540, 541, quoted from in our Opening Brief (from which Appellee also quotes). There it is said,

> "The general rule, without doubt, is, that no lapse of time or delay in bringing suit will be a bar to the remedy in equity, provided the injured party, during the interval, was ignorant of fraud, but the ignorance of such party must not have been negligent, for if by reasonable diligence fraud could have been discovered or ought to have been known, he will be deemed guilty of laches."

Therefore, under the doctrine of that case, which is the doctrine of the authorities generally, if the trustee was ignorant of the fraud and such ignorance was not due to lack of diligence in making inquiry and then reaching discovery, he is not barred by laches. If, on the other hand, he were guilty, then he is barred by the Statute of Limitations, (assuming that the Oregon statute is the applicable statute). Thus we repeat the question of laches in the case is academic, for it cannot be invoked, if we were without knowledge or were diligent; and if we had knowledge or

were negligent, there is no need to invoke it, for the statute of limitation then bars.

Moreover, in this case there is not a scintilla of evidence that the delay was working a hardship on defendant. True, according to the evidence, several men, as heretofore pointed out, have died—Arthur Spencer, Edward F. O'Flynn, Judge C. C. Carey, and Referee A. M. Cannon. But in no instance was there any testimony that any of these men had any knowledge concerning the transactions complained of, or that if they did, their testimony would have been helpful to Farrington.

Farrington, again and again in his Brief, stresses the inability which might be caused by lapse of time, to assemble evdence showing the value of the property which in our complaint it is alleged he purchased with his worthless Western Bond and Mortgage Company Stock, and which he immediately transferred out of his possession for the valuable Western Guaranty Company stock, thereby substituting these securities for the Western Guaranty Company Stock in the coffers of the Western Bond and Mortgage Company, retaining for himself the Western Guaranty Stock. Certainly he should be in a better position to establish the value of these securities and lapse of time should work to his rather than to the Trustee's benefit. But, be that as it may, there was no evidence introduced by or on behalf of Farrington and certainly there is no evidence in the record to establish the fact that the value of these securities would now be difficult to ascertain, or any more difficult than

they would have been within a reasonable time after the trustee discovered or should have discovered Farrington's fraud.

We conclude, therefore, as to the question of laches, that that doctrine has no place in this case—either in law or in fact.

DILIGENCE IN PURSUIT OF INFORMATION LEADING TO DISCOVERY

In his Brief (p. 37) Farrington indicates that a trustee in bankruptcy owes a greater diligence to make discovery than other litigants, and states further:

> "If he fails to take proper steps to secure all assets he is presumably negligent and may be charged with the value of the assets lost (re: Reinboth, 157 Fed. 627)."

Later, attention is called to the fact that the Trustee was an attorney, that he held himself out as a tax counselor, that he had the assistance of the Attorney General of the State of Oregon (presumably he meant the deputy Attorney General, Ralph Moody), of the Corporation Department of the State of Oregon, of two auditors of that Department, of Attorney John Latourette and Attorney Sidney Teiser, the latter of whom he generously denominated "one of the ablest bankruptcy attorneys practicing at this bar", and of Mr. Rudolph Erickson, a certified public accountant, (Appellee's Brief, pp. 40-41) whom he

falsely states "contracted to render services on all phases of the bankruptcy proceedings on a contingent basis." (He neither rendered, nor contracted to render any services on a contingent basis, nor did he contract to render services on *all phases of the bankruptcy proceedings.*)

Now, in light of the fact that a trustee can be charged with the value of assets which he negligently fails to recover for the estate, we ask, first, could McBride, under the facts of this case, be held liable for his failure to recover the assets here charged to have been extracted by Farrington? If not—and we, think the question answers itself—then he should not be chargeable with negligence in the failure to discover.

In view of the fact that McBride, himself, had legal and accounting knowledge, and had all the official and unofficial legal and accounting assistance outlined, we ask, secondly; is not such facts in themselves conclusive of the truth that he was not negligent in his efforts at discovery? On the other hand, does it not compellingly indicate that the truth was so shrewdly and deeply hidden in the books and otherwise by Farrington that it defied discovery by so many experts so long? Ought not McBride be commended for his zeal, and for ultimate discovery, rather than criticized and the creditors punished for his asserted neglect?

Much of Appellee's Brief, from p. 42 to the end, is taken up with an effort to indicate that the trans-

actions charged against Farrington in the plaintiff's complaint were not fraudulent, rather than in the discussion as to whether or not McBride was derelict in his duty to discover.

Much also of the Brief is taken up with a discussion of the postulate propounded by appellee that the whole question of the fraudulent character of the transactions is a question of the value of assets given and received. From which it is argued that since the accountant made no appraisal of the assets the Western Bond and Mortgage Company received, the Trustee was guilty of negligence.

For pages and pages of his Brief Appellee seems to forget that it is the trustee whom he must attack for the so-called lack of diligence, and not the Certified Public Accountant for his asserted inaptness or worse. We maintain that there is no evidence in the record of Accountant Erickson's lack of ability or segacity of or his carelessness. But, even if there were, certainly there was no evidence adduced that McBride was negligent in employing Erickson or that any information was brought home to him of Erickson's suggested unworthiness. Certainly McBride is not chargeable with the failure of the expert accountant to find or to report, if found, facts which should have led to discovery.

The books of the Bankrupt were punctilliously kept and were available, cries the appellee in his Brief. Further, he says, the books contained the data concerning the fraudulent transactions, and the trans-

actions were on the books to be read by any one who would read. However, the facts are that, to the extent of his ability, the trustee read them, two auditors from the Department of the Corporation Commissioner of the State of Oregon read them, the attorneys surveyed them, they were read by Erickson, a practicing Certified Public Accountant for over twenty years and a former member of the Oregon State Board of Accountancy (Tr. p. 140), and all that these experts and near experts read, did not bring to them the revelation of the fraudulent transactions alleged.

Ah!, says Farrington, but the agent of the United States Department of Internal Revenue discovered knowledge of the facts set forth in McBride's complaint, and if such agent could discover such facts, certainly all these other so-called experts should have done so, laying aside for the moment the fact that the revenue agent had available to him books and records of others to which the trustee's experts would not have available (and this, notwithstanding the statement of Farrington's Brief to the contrary). The trustee certainly is not chargeable with the fact that one man, through superior sleuthing or other abilities discovered a fact and others, presumably of like ability, did not discover such fact, at least in the absence of evidence that those whom the trustee employed were known to him to be incapable. The test is what a prudent man under the circumstances should do, and it is quite obvious that McBride acted prudently in employing what the appellee admits was the best legal talent and certainly in employing capable ac-

counting talent in his search for facts. But, the Appellee would have the Court believe that the trustee was negligent in discovering what the experts he employed could not find with the means available.

Now, we come to another question: What is it that Farrington claims McBride did, or failed to do that charges him with negligence in failure to discover?

The evidence shows that the trustee had available the books of account of the bankrupt. That certain newspaper articles came to the attention of the trustee and of his attorney, Mr. Sidney Teiser, in 1936 (Findings III, Tr. p. 73). These articles referred to certain suits brought against the Western Mortgage Company, as well as by that Company against others and that in one of the suits against the company, Farrington was made a party defendant. In this latter suit (Brockie v. Western Bond and Mortgage Co., Farrington et als) charges similar to those here made were contained in the complaint. This suit was dismissed on motion of Brockie. The testimony also showed that there was in existence the Revenue Agent's Report which uncovered the alleged fraud of Farrington, but such report was not in the files and records of the Western Bond and Mortgage Company and a copy of it was not obtained by the trustee until a few months before the institution of this suit. Testimony also showed that the trustee had legal council and accountant council and that he on several occasions caused to be conducted examinations under Section 21(a) of the bankruptcy act. The testimony

likewise showed that the trustee was not aware of what was contained in the revenue agent's report and that the reason that he did not see or obtain a copy of this report was that such copy was not in the files of the Western Bond and Mortgage Company and that there was no particular occasion for the trustee to obtain a copy of it, not knowing or having reason to believe what its contents were until the contest of the tax claim filed by the government became imminent. And the testimony also shows that the trustee was instructed by the referee not to precipitate a contest on the govcernment's claim for taxes by filing objections until monies or assets came into the estate sufficient to make the contest of the government's claim anything but academic, and that monies or assets did not come into the estate sufficient to pay expenses until a few months before the bringing of this suit, when final success resulted from the litigation instituted by the trustee against the Bank of California. This we believe is a fair summary of the evidence and there is no dispute concerning it and no contradictory evdence introduced.

Now, we repeat our question. In the light of these facts, wherein was the trustee negligent in his failure to discover? In addition to what has been stated herein it is claimed by Farrington that the trustee was negligent (1) in failing to follow through on the information obtained, and (2) in failing to obtain the revenue agent's report, for, says Farrington, if the Brockie and other complaints had been read and if the revenue agent's report had been scanned, knowl-

edge resulting in discovery or means of discovery would have come to the trustee when these complaints and this report should have been read. We answer. None of the suits except the Brockie suit against Farrington contains allegations leading to the facts alleged in the trustee's complaint, and that merely contained allegations concerning our first cause of action. The other suit, and there is only one other of them in the record, namely the suit of Thompson v. Western Bond and Mortgage Company, contains no allegation which would lead to a discovery of facts concerning the transactions here complained of. Now the Brockie suit was dismissed on motion of the plaintiff, Brockie, in 1931 (Ex. 71) The dismissal was granted over the protest of Farrington (See Defense Ex. 69) and only upon the payment by Brockie prior to its dismissal of a substantial cost bill including a special Master's fee. Now it is conceded that information as to this suit or of the contents of the complaint therein did not come to the trustee until 1936. For that matter, the trustee was not appointed until December 1934. Consequently, it wouuld have been obvious to the trustee had he made investigation in this suit any time after his appointment that Brockie, notwithstanding his allegations in the complaint, had dismissed the suit and had permitted the statute of limitations to run against it. Under the circumstances we maintain that a perusal of the files in the Brockie suit by the trustee would not have lead to any discovery herein for the trustee would have been, with the exercise of reasonable diligence, fully justified in

concluding that allegations contained therein were untrue or unprovable in the light of the fact that Brockie dismissed on his own motion his suit, even against the protest of Farrington and the other defendants and did nothing thereafter permitting the statute of limitations to run against him.

As to the alleged failure of the trustee to obtain earlier a copy of the revenue agent's report: We vigorously insist that in the exercise of due diligence the trustee was fully justified in his inaction in this regard. Of course, he had no knowledge that the agent's report on which an additional assessment was made would contain charges of fraud against Farrington or anyone else. In fact, he had no knowledge at all as to what it might contain except that it must have contained data justifying the agent to recommend additional assessment of taxes. Moreover, we maintain that when the trustee was instructed by the referee not to proceed with filing objection to the Government's claim for taxes or to attempt a contest thereof until money or property came into the estate with which to pay it, at least in part, that his inaction in obtaining earlier a copy of the agent's report was fully justified and, in that regard he was not negligent and did not fail to act with due diligence.

MISSTATEMENTS AND ARGUMENTS BASED ON MISSTATEMENTS

There are many mistatements and many argu-

ments based on misstatements or unjustified assumptions contained in the appellee's Brief. We shall not attempt to catalogue or to discuss all of them, but we shall content ourselves with but a few.

For example, it is said at page 39 of appellee's Brief,

> ". . . . at the time of his appointment and even before, plaintiff knew that Farrington and others were under a cloud of suspicion that he had caused assets of the corporation to be fraudulently disposed of."

There is not one scintilla of evidence in the record that McBride knew any such thing on or before his appointment as trustee. The fact is, the only intimation of fraudulent disposition of assets by Farrington was in a newspaper article, filed in 1936 as an exhibit in the case against the Bank of California, and as a matter of fact, the testimony shows that McBride never actually knew what was in this article, but accepted the chargeability of such knowledge to him because his attorney had cognizance of the article.

Again on page 39 in the Appellee's Brief it is stated:

> "Even a cursory examination of the bankrupt's books would have disclosed that shortly prior to the filing of the bankrupt's petition two large transfers of assets had been made (the transfers involved in this case) . . . . they were unusual transactions and out of the ordinary course of business and therefore challenged attention and investigation as a matter of course, particu-

> larly so because the entries disclosed that the Consolidated Credit Corporation Stock was exchanged for the Keystone stock which was owned by the Western Bond and (Tr. p. 144) Western Guaranty Stock was not transferred for money, but was exchanged for other assets."

These statements are not based on evidence. As a matter of fact, an examination of the books of the Western Bond and Mortgage Company will disclose that the transactions referred to were not unusual or out of the ordinary course of business as conducted by the Western Bond and Mortgage Company. There are multitudes of such transactions throughout its books. (See for some of them, the Revenue Agent's Report—Ex. 59.) Moreover, the entries do not disclose that the Keystone stock which was received for the Consolidated Credit Corporation stock was owned by the Western Bond and Mortgage Company, nor is there any reason why the entries on the books concerning these transactions should have a challenged attention and investigation as a matter of course. The entries merely showed that the Western Bond and Mortgage Company in the one instance was transferring some securities which it held (Western Guaranty Stock) for other securities of equal value. And, in the other instance that it was transferring certain securities which it held for other securities of equal value.

On page 41 of appellee's Brief it is said,

> "Mr. Moody, Assistant Attorney General, called upon plaintiff immediately after his appointment. . . . . He called his attention to the newspaper

accounts (Tr. p. 194) and the litigations in the state and federal courts charging Farrington with fraudulent transfer of assets including the transactions involved in this case."

And, again, at page 71 in the same connection the same statement is repeated in a changed language, this time as follows:

"The attention of the plaintiff was *specifically directed to these newspaper accounts* by Assistant Attorney General Moody immediately after plaintiff's appointment as receiver and subsequent thereto. Mr. Moody arranged that whenever there were any newspaper accounts pertaining to the affairs of the Western Bond that they were to be clipped and turned over to him and he in turn relayed them to the plaintiff . . . There is a large folder full of newspaper clippings in evidence."

We will quote the testimony of Mr. Moody,

"Q. Did you have any conversation with him respecting any civil or criminal liability that might attach to Mr. Farrington in respect to any prosecutions?

A. Well, I told him that he was to look into the matter very carefully and to collect all of the assets that were due. The corporation had created a lot of subsidiary corporations and I asked him to particularly look into that thing and to collect—to find out all of the assets that were due the comany.

I remember at one particular time there was The Bank of California matter and I understand that since they have had some judgment.

Q. I want to direct your attention particularly—

A. Oh, yes. Then, as far as Mr. Farrington was concerned, I know I called Mr. McBride's attention to the fact, I think, that Mr. Farring-

ton was interested in the original organization of the Western Bond and Mortgage Company, and the records showed that when they first made application to the corporation commissioner for a license to sell these securities he refused it, whereupon he proceeded to institute in the Circuit Court of the state—to apply for a mandamus compelling the corporation commissioner to accept their filing.

Q. Did you have any discussion with him respecting the lawsuits that had been brought in 1931, charging Mr. Farrington with having defrauded the company?

A. Well, there were some articles published in the newspaper at that time. The newspapers gave a great deal of publicity to this whole business, this whole transaction, and I was watching it very closely, and whenever there was some reference to some proceeding about Mr. Farrington, that was called to Mr. McBride's attention.

Q. By you? A. Yes. (Tr. 193-194)

(Cross Examination)

Q. You spoke of some papers, some articles being published in the newspapers and, that you saw the articles because you were interested. That was in 1934 that you are speaking of, articles appearing in the papers of 1934, is that right?

A. In answer to that, I wanted to say that I was quite interested in the case. It was a live case for me, and it had been assigned to me, and there was considerable publicity about the State intervening, and there was also considerable publicity in regard to the Western Bond and Mortgage Company, and I instructed all of them that whenever any article appeared in the paper about that to call my attention to it and, while I do not mean to say that I have any independent recollection about reading any article, I known whenever I did I came to Portland and spent

several days at a time talking to Mr. McBride, and his attention was always called to these things.

Q. What I am speaking about is that you referred to newspaper articles published concerning matters which had occurred after you became interested in the bankruptcy proceedings.

A. Yes, after I became interested.

Q. And not before 1934?

A. I, myself, knew nothing about the Western Bond and Mortgage Company until it was referred to me some time in 1934." (Tr. 199-200)

That is all the testimony of Mr. Moody on the subject, and it certainly does not bear out statements quoted from appellee's Brief. We particularly call attention of the Court to the fact that the newspaper articles referring to the Brockie suit (Ex. 64, 65 and 84—pp. 31, 32 and 84 of Appellee's Appendix of Exhibits), the Thompson suit (Ex. 75—p. 64 Appellee's Appendix), and the Pape suit (Ex. 85—p. 81 of Appellee's Appendix), *all appeared in the newspapers in 1931.* The only newspaper articles appearing in 1934 were articles concerning the bankruptcy cause itself. (See exhibits 78, 79, 80, 81, 82 and 83—pp. 69, 71, 74, 76, 77 and 78, Appellee's Appendix). So obviously the newspaper articles to which Mr. Moody called the Trustee's attention were not those concerning the suits to recover property fraudulently received by Farrington. Such articles appeared in 1931, three years previous.

Again on page 53 of the Appellee's Brief it is stated:

"The (Revenue Agent's) report is dated October

> 12, 1932, and it recites (p. 1) that the information contained in the report was obtained from *'an examination of the books and records of above named affiliated group.'* A reading of the report confirms the fact that it purports to show *only what is in the books."*

The Revenue Agent's report specifically indicates that there was an examination of the books of other companies than the Western Bond and Mortgage Company. For example, on page 2 of the report as copied into Appellee's Appendix of Exhibits it is said;

> "These transactions were reflected on taxpayers books *and upon the books of the Consolidated Credit Corporation* by a series of complicated book entries, and it was necessary to spend several days in analyzing the entries on the books of both companies to determine just what took place.

On page 3 of the agent's report, as reproduced in the Appellee's Appendix of Exhibits, it is stated:

> "The Consolidated Credit Corporation purchased the 150 shares of outstanding stock of the Consolidated Credit Company from the Western Bond and Mortgage Company, at a purported price of $75,000.00. This transaction was reflected on *its* books by the following entry."

and the entry indicates clearly that it was an entry *on the Consolidated Credit Company books.*

On page 9 of the Report, as reproduced in Appellee's Appendix of Exhibits, it is stated:

> "The tax liability accruing to the Laurel Invest-

> ment Company on this deal is being covered in a separate report on that company."

Obviously the revenue agent had to make an examination of the Laurel Investment Company books in order to make a report on that company.

The record itself, therefore, patently denies the statement made by Appellee in his brief that a reading of the report confirms the fact that it purports to show only what is in The Western Bond and Mortgage Company's books. It shows expressly that an examination of books of other companies were made.

The statement taken by appellant from the heading of the report, that,

> "An examination of the books and records of the above-named affiliated group for the calendar year 1930, disclosed the following in connection with its income tax liability"

was obviously not intended to be a statement that only the books of the taxpayer were being examined.

We shall desist from detailing other examples.

CONCLUSIONS

We assert therefore, that the evidence of record in this proceeding cannot justify the holding by the trial court that the trustee failed to exercise due diligence in earlier discovering the fraud of Farrington, set forth in the transactions alleged in his complaint.

We assert further that none of the derelictions

charged against the trustee applies to the second claim, viz., the transaction concerning the transfer out of the Western Bond and Mortgage Company of forty thousand shares of the Consolidated Credit Corporation stock for property already owned by the Western Bond and Mortgage Company.

We urgently insist that this case should be reversed and the cause remanded for trial on the question of fraud.

Respectfully submitted,

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